This was the basic logic, for example, of the Commission's price cap plan for LECs. Under price cap regulation, LECs may retain a significant portion of earnings above the level deemed "reasonable" (currently, 11.25%), as long as prices remain within the applicable caps. Such an arrangement creates incentives to improve efficiency and to invest in new technology.[43] Any number of state-level incentive regulation plans for telephone companies are based on the same premise.[44]

A key facet of these plans is the fact that normal telephone company operations will generate plenty of money to invest in system upgrades. Where telephone companies are generally flush with cash, however, cable operators often face adverse credit market conditions and severe cash shortages.[45] In order to achieve significant public benefits from new investments in the cable infrastructure, therefore, the Commission must recognize that cable operators, unlike telephone companies, may be unable to finance a system upgrade from the cash generated by that system.

As a result, if the Upgrade Incentive Plan is to work, the Commission must be willing to consider significant rate flexibility — including rate increases above the level needed simply to reflect inflation — for regulated cable services. Otherwise, it is hard to

---

[43] ***See supra*** n. 25.

[44] ***See, e.g.,*** In the Matter of the Application of New Jersey Bell Telephone Company for Approval of its Plan for an Alternative Form of Regulation, ***Decision and Order***, Docket No. T092030358 (May 6, 1993). Of course, in particular cases, regulators may well conclude that the public is better served by the rate decreases that traditional regulation would impose.

[45] ***See*** Comments of Cost-of-Service Parties at 59; Exh. G at 4, 25.

see precisely what meaningful "incentive" would be included in the Plan. More to the point, without additional rate flexibility, it is hard to see where the money will come from to fund the system upgrades in the first place.

One way to help mitigate the need for rate increases in an Upgrade Incentive Plan arrangement, at least for MSOs, would be to apply a single Upgrade Incentive arrangement on the level of the entire MSO. If the Commission were to approve an arrangement under which a cable operator serving multiple franchises could set the same rates for regulated services in all franchises, this would substantially reduce regulatory burdens on the operator, while allowing MSO-wide planning of system upgrades and MSO-wide capital budgeting.[46]

---

[46] Undersigned cable operators and associations have previously explained why, in general, the public interest would be served by allowing operators serving multiple franchises to offer services at average rates. Comments of Cost-of-Service Parties at 62. In fact, this Commission ***requires*** the use of averaged rates by telecommunications companies for most interstate toll and related services, and allows it for interstate access services. ***See, e.g.***, In the Matter of Expanded Interconnection with Local Telephone Company Facilities, Amendment of Part 36 of the Commission's Rules, and Establishment of a Joint Board, ***Second Report and Order and Third Notice of Proposed Rulemaking,*** 8 FCC Rcd. 7374 at ¶ 18(1993); In the Matter of The Mountain States Telephone and Telegraph Company, ***et al.,*** Revisions to Tariff FCC No. 1; Petition for Waiver of Section 65.702(c) of the Commission's Rules, ***Order,*** 4 FCC Rcd. 797 (1989). ***See also*** 47 C.F.R. § 65.702(c). Moreover, there is precedent for approving cable rates based on costs that are averaged over several communities. In a recent case under the 1984 Act, some municipalities complained that the cable operator serving them had not provided costs to justify rates on a franchise-specific basis. The court, however, approved the use of averaged rates. It recognized that franchise-specific rates might more precisely match the costs of serving particular customers with the rates those customers paid. Nevertheless, the benefits to all subscribers of operating a system serving many franchises on a consolidated basis justified the lack of precision. ***City of Ottawa, Illinois v. Sammons Communications,*** 836 F. Supp. 555, 559 (N.D. Ill. 1993).

B. The Commission Should Acknowledge Its Plenary Responsibility For Enacting Regulatory Policies That Facilitate The Development Of The National Information Infrastructure.

NATOA's statements[47] also highlight another concern. While most local franchising authorities are likely to take a fair and, indeed, supportive view of cable system upgrades that enhance the services available to their constituents, there may be some who might take an unduly narrow view, focusing only on the potential impact of an upgrade on the rates for the basic tier regulated services. The Commission should not countenance a situation where a backward-looking local franchising authority could potentially stymie a publicly beneficial upgrade by means of threats of a harsh regulatory response.

As a result, the Commission should consider, but not require, input from local franchising authorities as a precondition to considering a proposed arrangement under the Upgrade Incentive Plan. While local franchising authorities have a role to play in the regulation of cable rates, it is this Commission that has been given plenary authority over the cable television industry, including the contribution cable can make to the development of the National Information Infrastructure.[48] If, therefore, the Commission is presented with a proposed arrangement under the Upgrade Incentive Plan that is in the national public interest, it should approve that plan.

---

[47] Comments of NATOA at 2-3.

[48] ***See Cost-of-Service Order*** at ¶ 21 ("We adopt the goal of encouraging infrastructure investment and development").

The Commission should be particularly concerned with the allocation of the costs of system upgrades. If the costs of upgrading a system are unfairly allocated away from regulated services, this will create strong incentives for operators to focus their efforts to improve their services on offerings that are primarily deregulated. This would defeat the purpose of having an Upgrade Incentive Plan in the first place. As others have pointed out, a single-minded devotion to the lowest possible rates for regulated cable services is not in the public interest and, indeed, is contrary to the terms of the Cable Act itself.[49]

In this context, it is important for the Commission to clarify the approach that local franchising authorities must apply to the allocation of the costs of the system upgrade among regulated service tiers.[50] The Commission should hold that the costs of system upgrades shall be included in BBT rates in the same manner as the system's pre-upgrade costs. It should also expressly prohibit the use of artificial cost allocation methodologies that relegate an undue portion of system upgrade costs to the CPS tier or to unregulated services. While it is always possible to debate the degree to which individual customers or classes of customers might benefit from any specific upgrade, the public as a whole — including all existing customers — benefit from the deployment of optical fiber, improved system power and back-up power supplies, more sophisticated and reliable system electronics, increased channel capacity, and similar improvements.

---

[49] ***See*** Public Interest Petitioners, Petition for Expedited Reconsideration, MM Docket No. 93-215 (filed May 16, 1994) at 6-8.

[50] ***See*** Comments of NATOA at 3.

A ruling that the costs of general system upgrades should be included in regulated rates is also consistent with long-standing Commission precedent. When telephone companies began deploying Common Channel Signaling System No. 7 (SS7) technology in the mid-1980s, its most immediate application in the interstate arena was to improve the quality of toll-free "800" services. SS7 technology enabled local exchange carriers to implement an "800 data base" that would allow end users to retain their 800 numbers even while changing long distance carriers. Despite this relatively limited initial application, the Commission expressly rejected the claim that the interstate portion of SS7 costs should be allocated to specific access charge elements relating to 800 data base service.[51] Instead, the Commission held that the deployment of SS7 technology was a general network upgrade, the costs of which were properly spread among all users of the network. The only costs to be included in the specific "800 data base" rate elements were those related directly to the provision of that service.[52]

The same logic applies to cable system upgrades. All customers, whether purchasing primarily regulated services, primarily deregulated services, or an even mixture of both, benefit from general upgrades of the cable system serving them. As a result, the

---

[51] In the Matter of Provision of Access for 800 Service, ***Report and Order,*** 4 FCC Rcd. 2824 at ¶¶ 59-63 (1989).

[52] The only SS7-related costs assigned to the specific 800 data base access charge were "those costs ... incurred specifically for the implementation and operation of the data base system." ***Id.*** at ¶ 70.

Commission should reject any effort to allocate unfairly the costs of system upgrades and rebuilds away from regulated services.[53]

III. THE COMMISSION SHOULD REVISE AND IMPROVE THE PROCEDURES USED TO REVIEW COST-OF-SERVICE CASES.

GTE claims that the Commission should approve its cost-of-service rules as proposed.[54] In addition to the various substantive concerns with the rules discussed in our initial comments, events that have occurred since the filing of the initial comments demonstrate the need for improvements in some of the Commission's procedures for reviewing cable operator cost-of-service cases. Specifically, as the Cable Services Bureau staff began a detailed review of existing cost-of-service cases, it proved to be difficult to obtain a timely understanding of the additional information the Staff desired to aid in processing those cases.[55]

Some of the difficulties surrounding these matters apparantly arose, in part, from the fact that the Commission has been stretched thin with its new regulatory responsibilities and

---

[53] The need to allocate fairly the costs of an upgraded system among all customers also applies in the context of a normal cost-of-service proceeding, irrespective of any particular arrangement under the Upgrade Incentive Plan. ***See*** Comments of Cost-of-Service Parties at 29-32.

[54] Comments of GTE at 4-5.

[55] In some cases, the staff's specific requests were not received until after the close of business three business days before the information was due. ***See, e.g.,*** Supplemental Response Of Cable Equities Of Colorado, Ltd., d/b/a Northeast Gwinnett Cablevision And Rifkin Acquisition Partners, L.P., To The Complaint Regarding Cable Programming Services Provided In Gwinnett County, Georgia (filed July 14, 1994) at 1-4; Supplemental Response of United Video Cablevision, Inc., To The Complaint Regarding Cable Programming Services Provided In Breckenridge, Colorado (filed July 14, 1994); Supplemental Response of James Cable Partners, L.P., To The Complaint Regarding Cable Programming Services Provided In Union Point, Georgia.

only relatively recently has been able to hire sufficient staff to begin processing the cost-of-service cases already on file. The vagueness of the "general cost-of-service principles" standard applicable to those cases no doubt also played a role in complicating these matters.[56] Even so, the number of cost-of-service cases under the interim rules is likely to increase, if for no other reason than the fact that the additional rate reductions called for by the revised benchmark formula will push a number of systems previously on the margin between benchmark and cost-of-service rate justifications into the cost-of-service camp. As a result, the Commission should act now to improve the procedures used to review cost-of-service cases.[57]

First, the Commission should work with the industry to determine how much of the information called for by the Form 1220 is generally available, and in what level of detail, so that the Commission will receive the most relevant available information in the most useful format. In this regard, it is common for regulatory agencies engaged in cost-of-service ratemaking to establish standard filing requirements in cost-of-service showings, as well as standard formats for the presentation of the required information. For example, in the area of telephone regulation, for almost a decade the Common Carrier Bureau Staff, in

---

[56] The Cable Services Bureau was at some pains to explain that the data it was seeking in connection with cases to be evaluated under "general cost-of-service principles" was different from that required under the interim rules. ***See*** In the Matter of Cable Operator Rate Justification Filings, ***Order*** (released June 14, 1994).

[57] As we pointed out in our initial comments, the quality of regulatory decisions is generally enhanced by eliminating any concerns or ambiguities regarding the regulated firm's presentation, so that both the regulators and the firm may focus their attention on the real issues in the proceeding. ***See*** Comments of Cost-of-Service Parties at 73-77.

consultation with representatives of the affected telephone companies, has developed "Tariff Review Plans" in connection with significant tariff filings.[58]

For cable cost-of-service filings under the interim rules, a dialog with the industry may reveal areas where, for example, the Form 1220 calls for information at a greater level of detail than is needed to review and assess most cost-of-service filings. If so, in those areas a greater degree of aggregation may be appropriate. In other cases, if the Staff routinely discerns a need for additional and more detailed information with regard to particular entries on the Form 1220, amending it to require the more detailed information in all cases might be the best course. In all cases, the goal should be to "reflect[] both the specific information needed in light of ... relevant Commission rules and policies and the most effective and least burdensome methods of supplying this information."[59]

Second, the Commission should certainly permit, and perhaps should require, that the Form 1220 be filed on diskette in a standard format, in addition to or in lieu of

---

[58] ***See, e.g.,*** "Common Carrier Bureau Solicits Comments Regarding Modifications and Improvements to the Annual Access Tariff Review Plans," ***Public Notice,*** DA 93-1450, 8 FCC Rcd. 8484, 8484 (1993) ("In each of the last eight years, the Bureau has prepared TRPs, after consultation with the LECs and their customers, reflecting both the specific information needed in light of changes in relevant Commission rules and policies and the most effective and least burdensome methods of supplying this information."); In the Matter of Commission Requirements for Cost Support Material to be Filed with 1994 Annual Access Tariffs and for Other Cost Support Material, ***Order,*** 9 FCC Rcd 1060 at ¶ 5 (1994)("The modifications [to prior TRPs] we make were developed through informal discussions with telecommunications industry representatives and from comments suggesting improvements and modifications to the 1993 TRPs filed by interested parties."). Of course, it is highly unlikely that regulation of cable rates would require the volume of detailed information generally called for in connection with the review of telephone company rates.

[59] "Common Carrier Bureau Solicits Comments Regarding Modifications and Improvements to the Annual Access Tariff Review Plans," ***Public Notice,*** DA 93-1450, 8 FCC Rcd 8484, 8484 (1993).

whatever hard copy filing may be required. Electronic filing would not only facilitate review of what amounts to a complex spreadsheet, it would also tend to minimize problems and concerns arising from the transcription or mathematical errors that routinely accompany the preparation and review of hard copies of detailed financial presentations.

Third, the Commission should amend its rules to make clear that its staff, like the staff of a local franchising authority, is free to ask the affected cable operator questions regarding pending filings, and vice versa. There seems to have been some ambiguity on this issue because review of a cable operator's rates at the Commission is initiated by a document called a "complaint."[60] Clearly, however, a Form 329 is not a valid "complaint" in any meaningful sense. The information on a Form 329 does not establish a prima facie case, under any substantive ratemaking standard, that an operator's rates are too high. Viewed as actual ***complaints,*** therefore, Form 329s are not sufficient to create any obligation on the part of a cable operator to respond.[61]

The more apt procedural analysis is that, under the Cable Act of 1992, the filing of the "complaint" imposes an obligation on the Commission to begin an investigation of the

---

[60] Local franchising authorities, by contrast, review basic broadcast tier (BBT) and equipment rates on their own motion by certifying to regulate and requiring that the operator justify current rates or a proposed rate increase.

[61] In this regard, the Commission, on its own motion, revised the Form 329 to require even ***less*** information than had been required by the original form. Undersigned cable operators have significant concerns that the revised Form 329 does not include the minimal information identified by the 1992 Cable Act and by the Commission's rules. ***See*** 47 C.F.R. § 76.951(b)(6) (requiring "a description of the cable programming service or associated equipment involved and, if applicable, how the service or associated equipment has changed"; 47 U.S.C. § 543(c)(1)(B) (customer must make a certain "minimum showing" in order to obtain "Commission consideration and resolution of whether the rate in question is unreasonable").

reasonableness of the cable operator's rates.[62] Such a proceeding is best viewed as a traditional rate investigation, not as the adjudication of an actual "complaint" as such.[63] While cable operators' rates are not technically "tariffs," there are many practical similarities — including obligations of nondiscrimination, geographic uniformity, advance notice of price changes, and, most relevant here, cost-based justification of rates. For purposes of what procedures to apply, therefore, the procedures used to process tariffs provide a reasonable analogy.[64]

Irrespective of the precise procedural approach used, the Commission should revise its rules to allow the application in cable cost-of-service cases of procedures similar to those used to review telephone tariffs. These procedures would include, for example, an initial review of a cable operator's filing by the Commission's staff, followed by the

---

[62] As noted above, under the 1992 Cable Act, a "complaint" is the procedural device by which it is possible to "obtain Commission consideration and resolution of whether the rate in question is unreasonable." 47 U.S.C. § 543(c)(1)(B). This language does not call for trial-type "adjudication" of these proceedings.

[63] It has long been held that the process of setting rates is legislative, rather than adjudicatory, in nature. ***See, e.g., Munn v. Illinois,*** 94 U.S. 113 (1877). This basic doctrine has been cited approvingly by the Supreme Court as recently as this year. ***See Northwest Airlines, Inc. v. County of Kent,*** ___ U.S. ___, 114 S. Ct. 855, 127 L. Ed. 2d 183, 195 (1994), ***citing Colorado Interstate Co. v. FPC,*** 324 U.S. 581, 589 (1945).

[64] Courts have long noted the distinction between ordering reparations for charges above a previously approved rate, which is a quasi-adjudicative function, and setting appropriate rates in the first instance, which is a quasi-legislative function. ***See United States v. Central Truck Lines, Inc.,*** 548 F.2d 523 524-25 (5th Cir. 1977), ***citing Baer Brothers Mercantile Company v. Denver & Rio Grande Railroad Company,*** 233 U.S. 479 (1914) ("The Supreme Court ... has held that an order for reapartions is made by the Commission in its quasi-judicial capacity to rederss past overcharges ... while an order fixing new classification rates for the future is made in the exercise of the quasi-legislative function of the Commission ..."). The essentially "legislative" nature of the process by which the Commission reviews and sets cable rates strongly supports the conclusion that the more open and informal procedures applicable to "non-restricted" proceedings may properly be applied to Commission review of cable operator rates.

designation of particular issues for more detailed review, perhaps in the form of a specific "deficiency letter" to the affected operator.[65] Once these issues have been identified, the cable operator would be allowed a reasonable time to submit additional data. After the requested data have been submitted, the Commission's staff and the affected cable operators would meet, if need be, to ensure that all required data have been received in proper form, to provide additional data that might be needed, and to clarify any ambiguities that might exist in the filed information.

We are aware that, in its initial order regarding cable rate regulation, the Commission stated that its consideration of a rate complaint should be treated as a "restricted proceeding."[66] The basis for this conclusion was a concern that complainants and local franchising authorities, often without legal representation in Washington, D.C., would be unfairly disadvantaged as compared to cable operators if the more open procedures applicable to "non-restricted proceedings" were to be applied.[67]

Whatever validity this concern may have had in April 1993, it has been utterly overtaken by events in the context of the Commission's rules for cost-of-service regulation — which had not even been proposed at that time. Cost-of-service regulation is an extremely complex enterprise. In light of this complexity, it is the uniform practice for the

---

[65] ***See*** Comments of Cost-of-Service Parties at 74.

[66] In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 — Rate Regulation, ***Report and Order and Further Notice of Proposed Rulemaking,*** 8 FCC Rcd. 5631 at ¶ 357-62 (1993).

[67] ***Id.*** at ¶ 360.

staff of a regulatory body and representatives of the regulated firm to exchange information and discuss various aspects of the filing, whether as part of formal discovery procedures, informally, or, more commonly, both. These contacts may include both requests for additional information, discussion of information already submitted, or informal efforts to narrow or clarify areas of potential controversy. There is nothing improper or inappropriate about these contacts. To the contrary, they aid the regulatory body in reaching a prompt and just determination of the matter before it.[68]

Allowing such contacts is particularly important in cable cost-of-service cases because virtually all individual complainants, and even many local franchising authorities, will be without any background or expertise in the more arcane aspects of ratemaking, such as regulatory accounting, assessing a reasonable rate of return, determination of rate base and operating expenses (including appropriate adjustments), and cost allocation methodologies. To the extent that the Commission or its staff needs additional information or explanation of items relevant to cost-of-service ratemaking, therefore, the only realistic source will often be the affected cable operator or its representatives.

In this regard, even as it was ruling that consideration of rate complaints should be treated as restricted, quasi-adjudicatory proceedings, the Commission was quick to note that cable operators could make presentations to the Staff, at the Staff's request, as long as any

---

[68] ***See supra*** n. 63.

additional information provided was also served on the complainant.[69] We suggest that a reasonable modification to the current rules would allow contacts and submissions of additional information to be initiated by the affected cable operator (or by a complainant or a local franchising authority), as long as all parties are served with a notice of the contact.

As noted above, it is likely that there will be an increase in the number of cost-of-service cases pending before the Commission and local franchising authorities after the next major filing deadline has passed. For these reasons, the undersigned operators and associations urge the Commission promptly to clarify and improve the procedures that will apply to review of those filings, as described here and in our initial comments.

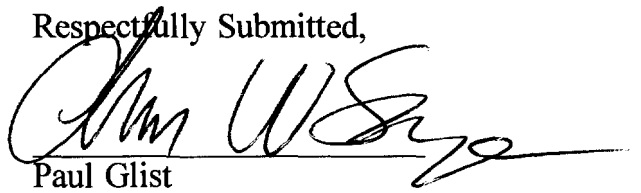
---

[69] In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 — Rate Regulation, ***Report and Order and Further Notice of Proposed Rulemaking,*** 8 FCC Rcd. 5631 at ¶ 362 (1993). This is the basis upon which discussions between representatives of cable operators and Cable Services Bureau Staff, referred to above, occurred.

IV. CONCLUSION

The Commission should modify its interim cost-of-service rules and adopt permanent rules consistent with the discussion in these Reply Comments, and in our initial Comments.

Respectfully Submitted,

By: 

Paul Glist
John D. Seiver
Christopher W. Savage
Frederick W. Giroux
COLE, RAYWID & BRAVERMAN

1919 Pennsylvania Avenue, N.W.
Suite 200
Washington, D.C. 20006
(202) 659-9750

Attorneys for Continental Cablevision, Inc., Crown Media, Inc., Jones Intercable, Inc., KBLCOM, Inc., Scripps Howard Cable Co., TeleCable Corporation, Greater Media, Inc., Rifkin & Associates, Inc., TCA Cable, Inc., Western Communications, Allen's TV Cable Service, Inc., American Cable Entertainment, Benchmark Communications, Brownwood Television Cable Services, Inc., CableAmerica Corp., CableSouth, Columbus Television Cable Corp., Daniels Cablevision, Inc., Gilmer Cable Television Co., Halcyon Communications, Inc., James Cable Partners, OCB Cablesystems, Inc., Sjoberg's Inc., Starstream Communications, United Video Cablevision, Zylstra Communications Corp.; Cable Television Association of Georgia, Cable Television Association of Maryland, Delaware and the District of Columbia, New Jersey Cable Television Association, South Carolina Cable Television Association, Tennessee Cable Television Association, Texas Cable TV Association.

August 1, 1994

CERTIFICATE SERVICE

I, Frederick W. Giroux, hereby certify that I have this 1st day of August, 1994, caused a copy of the foregoing to be delivered by first class mail, postage prepaid to the following:

Daniel L. Brenner
Counsel for the National Cable
Television Association
1724 Massachusetts Avenue, N.W.
Washington, DC 20036

Bruce D. Sokler
Mintz, Levin, Cohn, Ferris,
Glovsky and Popeo, P.C.
701 Pennsylvania Avenue, N.W.
Suite 900
Washington, DC 20004-2608

Stephen R. Effros
Cable Telecommunications Association
3950 Chain Bridge Road
P.O. Box 1005
Fairfax, VA 22030-1005

Melissa Newman
Wilkie Farr & Gallagher
Three Lafayette Centre
1155 21st Street, NW
Suite 600
Washington, DC 20036-3384

Leonard J. Kennedy
Dow, Lohnes & Albertson
1255 Twenty-third Street, N.W.
Suite 500
Washington, DC 20037

Stuart F. Feldstein
Fleischman and Walsh
1400 16th Street, N.W.
Suite 600
Washington, DC 20036

Certificate of Service (cont'd.)

Michael E. Glover
Edward Shakin
1710 H Street, N.W.
Washington, DC 20006

Robert L. Hoegle
Carter, Ledyard & Milburn
1350 I Street, N.W.
Suite 870
Washington, DC 20005

Norman Sinel
Arnold & Porter
1200 New Hampshire Avenue, N.W.
Washington, DC 20036

Theodore C. Whitehouse
Wilkie, Farr & Gallagher
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20036-3384

Andre J. Lachance
1850 M Street, N.W.
Suite 1200
Washington, DC 20036

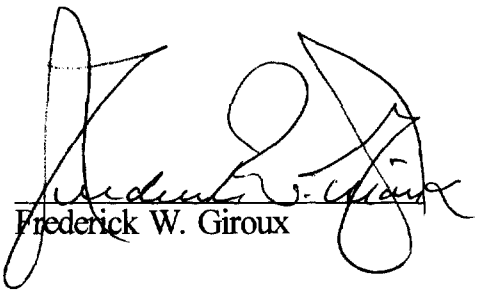
Richard W. Wiley
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, DC 20006

Howard J. Symons
Mintz, Levin, Cohn, Ferris,
Glovsky and Popeo, P.C.
701 Pennsylvania Avenue, N.W.
Suite 900
Washington, DC 20004

Certificate of Service (cont'd.)

Philip V. Permut
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, DC 20006

Judith A. McHale
Senior Vice President and
General Counsel
Discovery Communications, Inc.
7700 Wisconsin Avenue
Bethesda, MD 20814



Frederick W. Giroux